



STATE OF WASHINGTON

## ECONOMIC AND REVENUE FORECAST COUNCIL

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May 28, 2004

**TO:** Governor's Council of Economic Advisors

**FROM:** Chang Mook Sohn, Executive Director  
Office of the Forecast Council

**SUBJECT: PRELIMINARY MAY ECONOMIC FORECAST**

This preliminary forecast was based on Global Insight's May Control forecast for the U.S. economy. You should have received a summary of the Global Insight forecast by email. If not, please contact our office. The forecast incorporated the advance GDP estimate for the first quarter of 2003. According to the advance estimate, real GDP grew at a 4.2 percent rate in the first quarter of 2004. Payroll employment has now grown for two consecutive quarters, though only 0.6 percent and 1.0 percent. The forecast correctly assumed the Fed would leave its target rate unchanged at 1.00 percent in May. The forecast assumes the first rate increase will occur in August. The new national forecast is somewhat weaker than the forecast adopted in February particularly in employment growth. It should be noted that the forecast was released prior to May employment report which was much stronger than expected.

A comparison of the preliminary U.S. forecast with the forecast adopted in February is shown in Table 2.

The Washington State forecast reflects the slightly weaker growth in the new U.S. forecast. The Washington aerospace employment forecast is essentially unchanged. The forecast expects a decline of 2,200 during 2004 before a modest recovery begins in 2005 which adds 11,200 by the end of 2007. The software wage assumption has been lowered to reflect the assumption of lower stock option income. The software employment forecast assumes an increase of about 3,000 employees per year through 2007. Washington employment rose at a strong 3.1 percent annual rate in the first four months of 2004. As a result of the recent strength in employment, the population and housing forecasts have also been increased.

This forecast also incorporates newly available Covered Employment and Payrolls (ES-202) data for the fourth quarter of 2003. The benchmark revision to the fourth quarter added 8,200 to the level of employment in December. In addition, employment growth

from December through April was 10,300 higher than expected. The combined effect was an increase in April of 18,500. The ES-202 data also indicate that fourth quarter wages were \$0.842 billion lower than expected in February due mostly to a \$0.524 billion discrepancy in software wages. Non-software wages were also lower than expected by \$0.318 billion. Nonwage personal income was \$0.933 billion lower than expected in February due to historical revisions stemming from the comprehensive revision of the National Income and Product Accounts. The revision total personal income in the fourth quarter was a negative \$1.774 billion. The forecast also reflects Seattle consumer price data through April, which shows local inflation running well below the national average. Seattle's April-over-April core inflation was only 0.3 percent compared to 1.8 percent for the U.S. city average. The number of units authorized by building permit increased slightly in the first quarter to 42,000 from 41,000 in the fourth quarter of 2003.

A comparison of the preliminary Washington forecast with the forecast adopted in February is shown in Table 3.

Review of the forecast by the Governor's Council of Economic Advisors is scheduled for Friday June 4, 2004 at 10:00 a.m., in the **Insurance Building 4<sup>th</sup> floor conference room**.

If you have any questions, please contact Bret Bertolin, Senior Economic Forecaster, at (360) 570-6106.

**PLEASE NOTE:**

Enclosed is a worksheet summarizing the preliminary forecast. **Council members are strongly encouraged to complete and return this worksheet either in person at the Governor's Council meeting or, if unable to attend, by FAX to (360) 753-7022.** This worksheet is relied on by the Forecast Council members and staff to gauge the reasonableness of the preliminary economic forecast and also serves as the basis of an alternative economic and revenue forecast.

Fluctuations in software wages due to stock option income have, in the past, caused significant distortions in overall wage and personal income trends. The forecast assumes a rebound in option income in the second quarter of 2004 from an extremely low level in the first quarter. Nevertheless, lower stock option income in 2004 is expected to have a negative impact on wage and income growth in 2004 as shown in the table below.

Preliminary May Economic Forecast  
 May 28, 2004  
 Page Three

	2004:2	2004	2005	2006	2007:1,2
<u>Washington Real Personal Income, %Ch.</u>					
Baseline	5.1	2.7	3.9	4.5	4.1
Excluding Software	2.7	3.3	3.7	4.3	4.1
Software's Impact	2.3	-0.6	0.2	0.1	0.0
<u>Washington Average Annual Wage, %Ch.</u>					
Baseline	7.3	1.7	4.0	4.1	4.9
Excluding Software	2.8	2.9	3.8	3.9	5.0
Software's Impact	4.4	-1.1	0.2	0.2	0.0

CMS: dym/bb  
 Enclosures

Table 1  
**U.S. Economic Forecast Comparison**  
May 2004

	2004Q1	2004Q2	2004Q3	2004Q4	2004	2005	2006	2007
<b>Real GDP, Percent Change</b>								
Global Insight	4.2	5.0	4.8	4.3	4.8	3.6	3.4	3.3
Blue Chip	4.2	4.4	4.2	4.0	4.6	3.8		
Economy.com	4.2	5.1	4.5	3.5	4.8	3.5		
S&P	4.2	4.9	4.5	4.2	4.8	3.5	3.3	3.3
Merril Lynch	4.2	3.8	3.6	3.4	4.4	3.5		
<b>Federal Funds Rate</b>								
Global Insight	1.00	1.00	1.14	1.43	1.14	2.37	3.00	3.19
Blue Chip*	1.0	1.1	1.3	1.6	1.3	2.5		
Economy.com	1.00	1.02	1.16	1.46	1.16	3.00		
S&P	1.0	1.0	1.3	1.4	1.2	2.6	3.7	3.9
Merril Lynch	1.00	1.25	1.50	1.75	1.38	3.00		
<b>Consumer Price Index, Percent Change</b>								
Global Insight	3.6	3.2	0.9	1.4	2.2	1.5	1.4	1.9
Blue Chip	3.5	2.5	1.9	2.0	2.1	2.1		
Economy.com	3.6	2.1	1.4	1.3	2.0	1.3		
S&P	3.6	3.2	0.9	1.4	2.2	1.5	1.4	1.9
Merril Lynch	3.6	2.1	1.5	1.8	2.0	1.3		
<b>Payroll Employment, Millions</b>								
Global Insight	130.3	130.9	131.5	132.2	131.2	133.7	135.9	137.6
Economy.com	130.3	130.8	131.4	132.2	131.2	133.7		
S&P	130.3	130.9	131.5	132.2	131.2	133.7	135.7	137.3
<b>Unemployment Rate, Percent</b>								
Global Insight	5.63	5.63	5.52	5.49	5.57	5.48	5.46	5.40
Blue Chip	5.6	5.6	5.5	5.4	5.6	5.3		
Economy.com	5.6	5.7	5.7	5.7	5.7	5.7		
S&P	5.6	5.6	5.5	5.5	5.6	5.5	5.6	5.6
Merril Lynch	5.6	5.6	5.5	5.4	5.5	5.2		
<b>Real Disposable Personal Income, Percent Change</b>								
Global Insight	4.3	2.0	2.9	3.1	3.3	2.7	3.3	3.5
Blue Chip	4.3	3.9	2.8	3.8	3.8	3.4		
Merril Lynch	4.3	2.2	3.0	2.5	3.3	2.3		

\* Estimate based on T-bill rate.

Table 2

**U.S. Forecast Comparison**

	2003Q3	2003Q4	2004Q1	2004Q2	2004Q3	2004Q4	2003	2004	2005	2006	2007
<b>Real GDP (Billions of Chained 2000 Dollars)</b>											
May	10493.1	10600.1	10708.6	10840.1	10967.3	11082.4	10398.0	10899.6	11291.7	11676.0	12066.7
Percent Change	8.2	4.1	4.2	5.0	4.8	4.3	3.1	4.8	3.6	3.4	3.3
January	10493.1	10614.5	10719.7	10823.7	10956.0	11081.0	10401.6	10895.1	11325.9	11708.6	12089.4
Percent Change	8.2	4.7	4.0	3.9	5.0	4.6	3.2	4.7	4.0	3.4	3.3
<b>Implicit Price Deflator (2000=1.000)</b>											
May	1.055	1.058	1.066	1.074	1.077	1.081	1.053	1.074	1.091	1.108	1.132
Percent Change	1.8	1.0	3.2	2.9	1.1	1.5	1.8	2.0	1.5	1.6	2.1
January	1.055	1.056	1.060	1.062	1.065	1.069	1.053	1.064	1.079	1.098	1.123
Percent Change	1.7	0.2	1.8	0.7	1.2	1.5	1.8	1.1	1.4	1.8	2.2
<b>Real Personal Income (Billions of Chained 2000 Dollars)</b>											
May	8771.9	8851.7	8903.4	8954.9	9040.2	9121.3	8738.1	9004.9	9310.4	9675.1	10020.1
Percent Change	3.1	3.7	2.4	2.3	3.9	3.6	1.4	3.1	3.4	3.9	3.6
January	8758.8	8830.5	8900.3	8991.7	9092.0	9194.6	8729.5	9044.6	9420.7	9787.6	10140.3
Percent Change	2.5	3.3	3.2	4.2	4.5	4.6	1.3	3.6	4.2	3.9	3.6
<b>Wage and Salary Employment</b>											
May	129.82	130.00	130.33	130.85	131.48	132.16	129.94	131.20	133.69	135.89	137.59
Percent Change	-0.2	0.6	1.0	1.6	1.9	2.1	-0.3	1.0	1.9	1.6	1.2
January	129.90	130.11	130.54	131.47	132.47	133.38	130.06	131.96	135.41	137.70	139.67
Percent Change	-0.3	0.6	1.3	2.9	3.1	2.8	-0.2	1.5	2.6	1.7	1.4
<b>Unemployment Rate</b>											
May	6.13	5.87	5.63	5.63	5.52	5.49	5.99	5.57	5.48	5.46	5.40
January	6.13	5.87	5.81	5.72	5.61	5.48	5.99	5.65	5.30	5.29	5.27
<b>Mortgage Rate</b>											
May	6.01	5.92	5.61	6.11	6.27	6.37	5.82	6.09	6.48	6.59	6.74
January	6.01	5.93	6.15	6.31	6.61	6.78	5.82	6.46	6.99	7.04	6.98
<b>3 Month T-Bill Rate</b>											
May	0.93	0.92	0.92	0.93	1.10	1.37	1.01	1.08	2.19	2.76	2.93
January	0.93	0.92	0.97	0.98	1.42	1.60	1.01	1.24	2.17	2.73	2.91

Table 3

**Washington Forecast Comparison**

	2003Q3	2003Q4	2004Q1	2004Q2	2004Q3	2004Q4	2003	2004	2005	2006	2007
<b>Real Personal Income (Billions of Chained 2000 Dollars)</b>											
May	196.890	194.363	195.695	198.144	200.577	202.476	193.995	199.223	206.897	216.105	225.371
Percent Change	5.9	-5.0	2.8	5.1	5.0	3.8	1.3	2.7	3.9	4.5	4.3
January	198.518	196.422	199.343	201.265	203.409	205.564	195.834	202.395	210.335	219.081	228.574
Percent Change	5.7	-4.2	6.1	3.9	4.3	4.3	2.2	3.4	3.9	4.2	4.3
<b>Personal Income</b>											
May	207.753	205.604	208.640	212.774	215.962	218.794	204.322	214.043	225.714	239.562	255.169
Percent Change	7.7	-4.1	6.0	8.2	6.1	5.3	3.2	4.8	5.5	6.1	6.5
January	209.470	207.378	211.392	213.797	216.695	219.829	206.158	215.428	227.056	240.661	256.636
Percent Change	7.6	-3.9	8.0	4.6	5.5	5.9	4.0	4.5	5.4	6.0	6.6
<b>Wage and Salary Employment</b>											
May	2660.1	2669.5	2686.1	2704.3	2717.5	2732.4	2658.3	2710.1	2769.5	2827.2	2879.5
Percent Change	1.7	1.4	2.5	2.7	2.0	2.2	0.2	1.9	2.2	2.1	1.8
January	2659.9	2665.6	2670.4	2687.6	2706.6	2723.6	2658.3	2697.1	2764.4	2821.8	2879.2
Percent Change	1.2	0.9	0.7	2.6	2.9	2.5	0.2	1.5	2.5	2.1	2.0
<b>Manufacturing Employment</b>											
May	264.9	262.9	262.5	261.9	261.1	258.6	266.9	261.0	262.5	268.6	275.3
Percent Change	-3.9	-3.0	-0.6	-0.9	-1.2	-3.8	-6.4	-2.2	0.5	2.3	2.5
January	265.0	261.9	260.9	260.8	260.0	258.6	267.3	260.1	261.3	268.2	274.6
Percent Change	-5.3	-4.6	-1.5	-0.1	-1.3	-2.1	-6.4	-2.7	0.5	2.6	2.4
<b>Construction Employment</b>											
May	156.3	157.7	161.4	164.4	165.1	166.4	155.8	164.3	169.3	173.3	177.1
Percent Change	4.9	3.7	9.7	7.8	1.8	3.2	1.1	5.5	3.0	2.3	2.2
January	156.3	158.4	159.4	160.0	160.3	161.3	156.3	160.2	164.4	168.2	172.4
Percent Change	3.4	5.6	2.5	1.4	0.7	2.6	1.2	2.5	2.6	2.3	2.5
<b>Housing Permits</b>											
May	44.783	41.024	42.007	44.310	44.022	43.834	42.825	43.543	44.507	43.408	42.566
Percent Change	25.1	-29.6	9.9	23.8	-2.6	-1.7	6.5	1.7	2.2	-2.5	-1.9
January	45.258	40.966	40.952	40.455	41.004	41.368	43.159	40.945	40.570	39.160	40.450
Percent Change	24.6	-32.9	-0.1	-4.8	5.5	3.6	7.4	-5.1	-0.9	-3.5	3.3

Advisor's Name: \_\_\_\_\_

**Forecast Worksheet**  
**June 4, 2004**

	2004:Q2	2004	2005	2006	Average 2007:1,2
<b><u>U.S.</u></b>					
<b>Real GDP, %Ch</b>					
Baseline	5.0	4.8	3.6	3.4	3.3
Your Opinion	_____	_____	_____	_____	_____
<b>Implicit Price Deflator, % Ch</b>					
Baseline	2.9	2.0	1.5	1.6	2.2
Your Opinion	_____	_____	_____	_____	_____
<b>Mortgage Rate, Percent</b>					
Baseline	6.1	6.1	6.5	6.6	6.6
Your Opinion	_____	_____	_____	_____	_____
<b><u>Washington State</u></b>					
<b>Real Personal Income, % Ch</b>					
Baseline	5.1	2.7	3.9	4.5	4.1
Your Opinion	_____	_____	_____	_____	_____
<b>Wage and Salary Employment, % Ch</b>					
Baseline	2.7	1.9	2.2	2.1	1.7
Your Opinion	_____	_____	_____	_____	_____
<b>Manufacturing Employment, % Ch</b>					
Baseline	-0.9	-2.2	0.5	2.3	2.1
Your Opinion	_____	_____	_____	_____	_____
<b>Construction Employment, % Ch</b>					
Baseline	7.8	5.5	3.0	2.3	2.3
Your Opinion	_____	_____	_____	_____	_____
<b>Housing Permits (Thousands)</b>					
Baseline	44.3	43.5	44.5	43.4	42.9
Your Opinion	_____	_____	_____	_____	_____
<b>Washington Average Annual Wage, % Ch</b>					
Baseline	7.3	1.7	4.0	4.1	4.9
Your Opinion	_____	_____	_____	_____	_____